

## Quarterly Investment Summary – 31 July 2016

The dominant issue influencing global financial markets over the summer was the UK's referendum vote to leave the European Union (EU). The decision to leave took markets by surprise and led to a period of heightened volatility as investors sought to interpret its impact. All major asset classes were affected by the referendum and, in the UK, sterling in particular weakened. Central Banks also took stock – the Federal Reserve decided to delay further rate hikes until the economic picture became clearer, while both the Bank of England and ECB stood ready to act in support of financial stability.

In UK politics, the referendum result led to a dramatic unravelling on both the right and the left: the Prime Minister, David Cameron, resigned while Jeremy Corbyn suffered a vote of no confidence from the Labour Parliamentary Party. To provide market reassurance and avoid any prolonged political uncertainty, the Government quickly elected a new Prime Minister, Theresa May, who is now tasked with triggering Article 50 of the Lisbon Treaty before guiding the UK through crucial EU exit negotiations.

Despite the uncertainty created by the referendum, positive data over the review period showed that, against a background of subdued inflation, the global economy remained in good health reflected in robust US consumer spending and solid labour market growth, plus expanding economies in both the UK and Eurozone. Elsewhere, China continued to stabilise as it re-structures towards a consumer-led economy, while improved corporate earnings and a reformist Government suggested that the worst of the recession was over in Brazil, Latin America's largest economy. Initial signs post-EU referendum point to UK and European economies being most affected by the result, while North American, Asian and Emerging Markets appear most insulated from its impact.

<b>Consensus Economics</b>				
	<b>2015 Actual</b>		<b>2016 Consensus forecasts (Invesco forecasts)</b>	
<b>Economies</b>	<b>Real GDP (%)</b>	<b>CPI Inflation (%)</b>	<b>Real GDP (%)</b>	<b>CPI Inflation (%)</b>
US	2.4	0.1	1.8 (1.8)	1.3 (1.1)
Eurozone	1.6	0.0	1.5 (1.6)	0.3 (0.2)
UK	2.3	0.1	1.4 (1.6)	0.8 (0.7)
Japan	0.6	0.8	0.5 (0.7)	-0.1 (-0.2)
Australia	2.5	1.5	2.9 (2.7)	1.4 (1.3)
Canada	1.1	1.1	1.4 (1.6)	1.6 (1.1)
China	6.9	1.4	6.6 (6.6)	1.9 (1.6)
India	7.6	4.9	7.6 (7.5)	5.1 (5.1)

*Source - Consensus Economics, Survey Date: 7 June 2016. Figures for UK, Eurozone & US include post-Brexit data reported on 28 June 2016*

## Market Reaction

The immediate aftermath of the UK's decision to leave the EU saw global stock markets tumble – the FTSE 100 was down at one stage over 8% - but, as fears over the outcome eased, equities participated in a post-EU referendum rally to end the review period in positive territory.

In the UK, medium and smaller sized firms were initially aggressively sold off while sectors hardest hit were typically among financial (banks, insurance & property) stocks and construction firms as investors switched into 'defensive' areas such as tobacco & health care. By the end of July, however, cheaper valuations and reduced concern over Brexit ensured that equities generally finished higher than before the referendum. Sterling's weakness further supported higher share values for UK companies with overseas revenue streams, notably in the FTSE 100. Outside the UK, major equity markets rose over the review period with the best gains coming from North American, Asian and Emerging Markets.

In response to uncertainty arising from the referendum, a so-called 'flight to quality' saw traditional 'safe havens' strengthen such as Government debt, gold and currencies like the US Dollar and Japanese Yen. Indeed, post referendum, yields on Government debt in Europe and North America reached record lows, making the asset class increasingly less attractive, while the UK commercial property market suffered as investors questioned whether the asset class would retain its value after Brexit.

## Outlook

After the initial shock over the EU referendum, markets settled before gaining upward momentum as investors were ultimately guided by economic fundamentals rather than sentiment. Growth in the UK economy may slow in the next few months, but for other major economies, growth remains on track, supported if necessary by Central Banks.

## Fund Manager Meetings

As part of our research process, we regularly meet fund managers to gather information on markets, funds, sectors and asset classes. Below are some comments on recent meetings:

Ewan Markson-Brown, co-manager of **Baillie Gifford Pacific**, updated us in May on his fund's progress. In common with Baillie Gifford's house style, the Pacific fund is a long term investor, holding companies for at least three to five years, with a preference for medium-sized firms. Ewan and co-manager Roderick Snell do not 'hug' any benchmark such is their confidence in stock selection which has particular emphasis on themes such as technology, demographics and economic reform. Over the last five years Baillie Gifford Pacific has built a strong performance record and is positioned to gain further from economic development in Asian and Emerging Markets.

Since December 2010, Chris White has managed **Premier Income**, successfully constructing a high conviction portfolio of 40 – 50 stocks selected from across the broad market. Having previously worked at Threadneedle and Legg Mason, Chris is an experienced equity income manager whose reputation in recent years has grown thanks to his fund's consistently strong performance relative to its peers.

In the smaller company space, we recently met Mark Nizhnik, manager of **Artemis UK Smaller Companies**. Mark constructs a diversified portfolio of stocks with a 'defensive' bias in areas like Health Care and Beverages. Whilst previously working at Standard Life, Mark produced outstanding returns running their UK Opportunities fund, but since joining Artemis in October 2007, just before the financial crisis, he has struggled to replicate his former success.

At a post-Brexit investment conference in Bath, we met John Baker, manager of **JPMorgan UK Dynamic**. Johns invests in companies which meet his three core principles – value, quality and momentum - essentially, he buys companies which he believes are attractively valued and which have sustainable and growing earnings. Ahead of Brexit, John reduced risk in his fund, but has maintained a cyclical tilt in the belief that the UK economy may slowdown, but will not go into recession. Despite its focus on the FTSE 100, the fund has suffered short term from a high cash weighting. Over the longer term, however, performance remains positive.

<b>Asset Performance Table - figures to 31 July 2016</b>			
	<b>Three months</b>	<b>One Year</b>	<b>Three Years</b>
	<b>%</b>	<b>%</b>	<b>%</b>
<b>Equities</b>			
MSCI United Kingdom	<b>8.8</b>	<b>4.3</b>	<b>12.3</b>
MSCI North America	<b>16.4</b>	<b>22.4</b>	<b>50.4</b>
MSCI Europe ex UK	<b>9.4</b>	<b>5.9</b>	<b>19.9</b>
MSCI Japan	<b>13.4</b>	<b>13.4</b>	<b>30.9</b>
MSCI Pacific ex Japan	<b>16.4</b>	<b>18.6</b>	<b>22.2</b>
MSCI Emerging Markets	<b>16.0</b>	<b>16.7</b>	<b>13.2</b>
<b>Government Debt</b>			
UK Gilts <sup>1</sup>	<b>9.7</b>	<b>14.0</b>	<b>28.0</b>
US Treasury (US\$) <sup>2</sup>	<b>0.4</b>	<b>2.0</b>	<b>7.0</b>
<b>Commodities</b>			
Brent Crude (US\$)	<b>-8.1</b>	<b>-17.6</b>	<b>-59.3</b>
Gold (US\$)	<b>5.2</b>	<b>24.0</b>	<b>3.4</b>
<b>Currency Markets - Sterling vs Major Currencies</b>			
Sterling	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>
US Dollars	<b>10.3</b>	<b>17.5</b>	<b>14.2</b>
Euros	<b>7.7</b>	<b>19.0</b>	<b>-3.8</b>
Japanese Yen	<b>15.2</b>	<b>42.1</b>	<b>9.6</b>
<b><sup>1</sup> FTSE UK Gilts All Stocks Index, <sup>2</sup> US Treasury 10 Year Bill</b>			
<b>All figures - cumulative total returns, sterling adjusted unless stated @ 31 July 2016.</b>			<b>Source - FE Analytics</b>

Information and opinions contained herein have been compiled or arrived at by Belgrave Asset Management Limited and are provided solely to enable our clients to make their own investment decisions. They do not constitute a personal recommendation to invest. Past performance is not necessarily a guide to future performance. The value of investments and the income from them can go down as well as up and investors may not get back the amounts originally invested. Exchange rate changes may cause the value of overseas investments to rise or fall. Belgrave Asset Management Limited, Sterling House, Upper Bristol Road, Bath BA1 3AN, registered in England No. 3936094 is authorised and regulated by the Financial Conduct Authority